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February 27, 2025

*Via E-mail*

Assemblymember J. Gary Pretlow, Chair  
Standing Committee on Ways and Means  
The New York State Assembly

Senator Liz Krueger, Chair  
Standing Committee on Finance  
The New York State Senate

### **Re: COST Seeks Revisions to Executive Budget Part V – New York Should Adopt MTC Consensus Model to Report Federal Tax Adjustments**

Dear Chairs Pretlow and Krueger:

I am writing on behalf of the Council On State Taxation (“COST”) and respectfully suggest changes to Part V of the Executive Budget (“Executive Budget”) to conform its language to the Multistate Tax Commission’s (“MTC”) Consensus Model Legislation (attached) for reporting federal tax changes, including partnership adjustments.<sup>1</sup> As proposed in the Executive Budget, Part V fails to adequately address the reporting of federal tax adjustments, which is an issue raised in COST’s “Best and Worst of State Tax Administration – COST Scorecard on State Tax Appeals & Procedural Requirements.”<sup>2</sup> COST and other interested parties (*e.g.*, Tax Executives Institute and American Institute of Certified Public Accountants) worked on the MTC Consensus Model legislation to improve the overall process for all taxpayers, including partnerships subject to a 2015 federal law change that significantly modified the procedures for the Internal Revenue Service to audit and process many partnership tax changes for tax return years beginning on and after January 1, 2018.

### **About COST**

COST is a nonprofit trade association based in Washington, DC. COST was formed in 1969 as an advisory committee to the Council of State Chambers of Commerce and today has an independent membership of approximately 500 major corporations engaged in interstate and international business, many of which directly conduct business in New York. COST’s objective is to preserve and promote the equitable and nondiscriminatory state and local taxation of multijurisdictional business entities.

<sup>1</sup> New York is an Associate Member of the MTC.

<sup>2</sup> COST’s Administrative Scorecard is available at: <https://www.cost.org/globalassets/cost/state-tax-resources-pdf-pages/cost-studies-articles-reports/cost-2023-admin-scorecard---final-draft-combined.pdf>

### **COST Policy Position on Reporting Federal Tax Changes**

The COST Board of Directors has adopted a formal policy position for reporting federal tax changes.<sup>3</sup> That policy position provides:

*State<sup>4</sup> reporting of federal tax changes imposes a significant compliance burden on multijurisdictional companies. A fair and efficient state procedure for reporting federal tax changes should include: 1) a clear definition of what constitutes a “final determination” that triggers a state reporting requirement; 2) a minimum period of at least 180 days (or six months) to report such changes to the state; 3) conformity to the Multistate Tax Commission model statute for reporting and payment of partnership audit adjustments; 4) the ability to make advanced payments before a “final determination” triggers the filing responsibility for an amended return; and 5) a limitation on issues open for adjustment to those items that are altered as a result of the federal change (after the normal statute of limitations has expired).*

While Part V of the Executive Budget attempts to make some changes to address the reporting of federal partnership tax adjustments, it fails to make the necessary improvements to those provisions to comport with COST’s policy statement and the MTC Consensus Model legislation (including partnerships).

### **Improvements Needed to Improve the Reporting of Federal Adjustments**

The following are some necessary enhancements (not inclusive) to improve taxpayers’ reporting of federal adjustments to the New York Department of Taxation and Finance (all addressed in the MTC’s Consensus Model Legislation):

- Increase the time to report federal adjustments from 60 days to 180 days (interest is still owed on any additional tax due);
- Clearly allow estimated payments for taxpayers under federal audit to report estimated State tax liability, with a clear provision that allows a refund of any overpayment;
- Use the MTC’s model for what constitutes a “final determination,” requiring the “trigger” to be based on all members of a combined group having finalized their IRS audits;
- Provide a *de minimis* exception for filing amended returns if such liability is insignificant;
- Clarify a federal partnership representative binds a partnership under a federal audit applies to the State, with procedures for the partnership to separately designate a different state partnership representative;
- Follow the MTC Consensus Model Legislation that defaults to partners reporting changes and the partnership having the ability to elect to pay the tax for its partners;
- Have clear procedures for a partnership to directly remit the tax, including tiered partnerships; and

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<sup>3</sup> COST’s Policy Position on “Reporting Federal Tax Changes” is available at: <https://www.cost.org/globalassets/cost/state-tax-resources-pdf-pages/cost-policy-positions/cost-federal-tax-changes-rar-policy-december-2023.pdf>

<sup>4</sup> As used in this policy statement, “state” refers to both state and local jurisdictions impacted by federal tax change reporting requirements.

- Provide a 60-day waiver for partnerships with over 10,000 partners to report changes.

### **Conclusion**

For the reasons discussed above, COST urges your committees to revise and amend the Executive Budget, Part V, to conform with the MTC Consensus Model. Please let us know if we can assist in making these changes and if you have any questions.

Respectfully,

  
Leonore F. Heavey

cc: COST Board of Directors  
Patrick J. Reynolds, COST President & Executive Director  
Amanda Hiller, Commissioner, New York State Department of Taxation and Finance

Attachment.

# **Model Uniform Statute for Reporting Adjustments to Federal Taxable Income and Federal Partnership Audit Adjustments**

## **DRAFT – With Technical Correction as of November 2020 and Additional Note for States Adopting the Model**

### **Technical Correction Adopted November 2020**

The technical corrections to this model involve negative federal adjustments—that is, changes in federal tax items which would result in overpaid state tax. Assuming that these negative federal adjustments cannot be completely netted against any positive federal adjustments under IRC section 6225(b) in computing an imputed underpayment—they may be treated in one of two ways. In general, audit adjustments subject to IRC section 6225(a)(2) will be “taken into account by the partnership in the adjustment year.” This means they will be included as items on the partnership return filed in the year of adjustment, offsetting other related items of income from that year, which will then be allocated to partners in that year. See 26 CFR § 301.6225-3. In contrast, negative federal adjustments reported by the partnership through an Administrative Adjustment Request (AAR) will be “pushed out” under Section 6227 and 6226. Under the push-out method, the adjustment does not flow through the partnership return but is, instead, separately allocated to the reviewed year partners who calculate the overpaid tax for the year to which the AAR relates and then report the overpaid tax amount as a credit on their federal tax returns in the year of adjustment.

In the same way that states need a method for assessing any state tax where a positive federal adjustment is pushed out to the partners, they need to provide a method for claiming any refund of state tax, otherwise allowable, where a negative federal adjustment is pushed out. See Section G of the model. But to allow partners to separately apply for a state tax refund where the negative federal adjustment is taken into account on the partnership’s adjustment year return would result in double-counting of those adjustments (unless states also decoupled from using the federal partnership return and Schedule K-1s as the starting point for state filing). Therefore, the model excluded these negative federal adjustments from its provisions, including Section G.

In excluding these negative federal adjustments, the model simply referenced IRC section 6225(a)(2), rather than describing the basis for the exclusion—that is, that the adjustments are “taken into account by the partnership in the adjustment year.” It appears, however, that in some cases, the IRS may, by regulation, vary the negative federal adjustments that will be “taken into account by the partnership in the adjustment year.” In addition, Section G of the model did not clearly provide for claiming state tax refunds based on negative federal adjustments resulting from Administrative Adjustment Requests (AARs) at the time the AAR is filed, because it used the term “made by the IRS.” This led to some confusion over the intention of Section G.

The technical corrections remove the citation to IRC section 6225(a)(2), in Section G and other places in the model, and replace that reference with the language from that provision—adjustments “taken into account by the partnership in the adjustment year.” This will clarify that it is *those* adjustments which are not subject to either separate reporting or a separate state tax refund claim. The technical corrections further include “Administrative Adjustment Requests” in the title of Section G and remove the reference to “made by the IRS.” This clarifies that those negative adjustments resulting from an AAR filed by the partnership may be the basis for a state tax refund claim (provided they are not “taken into account by the partnership in the adjustment year”).

In addition, to these technical corrections, there is one other technical correction of note in Section C(5). This provision allows the state revenue agency to develop an alternative reporting process in response to requests from partnerships. The technical correction to that section would provide for the partnership to also claim a refund “if the Audited Partnership or Tiered Partner can show that their direct partners have agreed to allow a refund of the state tax to the entity.” Section G then provides that in such case—“Any refund granted to the entity under Section C is in lieu of state tax that may be owed to the partners.” In addition, a drafter’s note was added in the text of this section noting that the intent of this provision is to provide the agency with authority for alternative reporting provided such alternative reporting would otherwise conform to state law.

### **Additional Note for States Adopting the Model**

As of November 2020, there are still states that have not adopted the model or similar provisions. It is possible that Administrative Adjustment Requests may be filed reflecting positive or negative federal adjustments before the effective date of state law. States should therefore consider modifying the definition of the term “final determination date” to include a date certain, extending the final determination date, for federal adjustments that result from actions prior to the effective date. For example, a state may consider modifying the definition of “final determination date” to include such language as: . . . the Final Determination Date is *the later of the effective date of this Act or . . .*”.

### **Drafters’ Notes**

Certain provisions of this model, particularly Section C, were drafted by the Commission’s Uniformity Committee in anticipation of federal audits that will be done through the new centralized partnership audit regime beginning for 2018 tax years. These provisions are necessary because states otherwise lack the means to require reporting of, or to assess taxes related to, partnership audit adjustments where the federal tax is assessed to and paid by the partnership or is “pushed-out” to the partners in adjustment-year returns. This model also updates provisions of the Commission’s 2003 Model Uniform Statute for Reporting Federal Tax Adjustments.

The drafters concluded that states could not effectively implement a “push-out” approach

similar to the federal approach, for various reasons. But Section C does include a partnership-pays election for paying state taxes owed on federal partnership audit adjustments. In drafting the provisions of this election, it was recognized that, with respect to “tiered partners,” the electing partnership may not have sufficient information to source the adjustments allocated to those partners—particularly information on the residency status of the tiered partner’s individual partners (“indirect partners”). Therefore, if a federal audit adjustment relates to a type of income that is sourced 100% by the state based on residency (rather than apportioned), the calculation of the partnership-pays amount effectively assumes that indirect partners are residents so that 100% of the adjustment would be sourced to the state for those tiered partners. See Section C(3)(b)(iv)(B). Nor would the tiered partner’s indirect partners be allowed a credit for taxes paid to another state. If the partnership wishes, instead, to apportion any part of these types of adjustments when allocated to tiered partners, it will have to provide information on the residency of the tiered partner’s taxpaying partners. See Section C(3)(b)(iv)(C).

Throughout the model, references to existing state laws of the adopting state must be included. Particularly in the partnership pays election, there are references to state law governing the sourcing of multistate income (allocation and apportionment rules). The model does not constrain the states in applying particular sourcing rules nor does it require the states to apply uniform rules. Those rules can also change over time. And, to the extent that there are specific rules for apportioning partnership income or certain types of income, those rules would apply in the partnership-pays election context. Such rules might also include equitable apportionment provisions. The only requirement is that the rules generally applicable in the reviewed year (audit year) be applied to adjustments for that year.

Note that certain provisions of the model specify that regulations should be promulgated to implement those provisions. Other regulations, or agency instructions, may be necessary, as well, to fully implement the model. The model was drafted in this manner, in part, to retain some flexibility, recognizing that the provisions related to partnership audit adjustments are new and untested. In addition to the provisions that specifically call for regulations, states may wish to consider regulations or instruction to:

- Define the precise information required to be provided in a federal adjustments report, generally, and specifically in the case of federal partnership adjustments that must be reported by the partnership under Section C(2).
- Specify the manner in which federal adjustments, and especially federal partnership adjustments, might need to be modified in order to conform to state tax laws (e.g. where an add-back statute might apply to an adjusted item or where that item has no impact at the state level) including how those modifications would be reported by the partnership.
- Specify the information that would be required for a partnership electing the partnership-pays approach to overcome the presumption that, in some cases, the indirect partners are residents, and the manner of requesting other

adjustments in the partnership-pays approach. Section C(3)(b)(iv)(C) and Section C(5).

- Define how adjustments determined to be unitary business income of a corporate partner should be reported and treated by that partner where the partnership makes the partnership-pays election. Section C(3)(c).
- Determine the manner of allowing credits for taxes paid to other states by the partnership for its direct resident partners. Section C(6)(b).
- Specify the manner for making estimated payments as provided for in Section F during the course of a federal audit.

Also note that the draft contains a definition of “reallocation adjustment” which was originally included with the expectation that states might treat reallocation adjustments differently. Ultimately, it was determined that the states ought to follow the federal treatment of reallocation adjustments (including the tax-positive side in the partnership pays amount, but not the tax-negative side); however, the definition was not removed.

Finally, the partnership-pays election may potentially have revenue impacts. In some cases, the tax paid under that election to the state would be greater (primarily because of the use of the highest marginal rate to compute the tax). The revenue may also be greater if a partnership generates income that would ordinarily be sourced to the state of residence, and if that partnership has indirect partners. In that case, the indirect partners would be presumed to be resident partners for purposes of computing the partnership-pays amount unless the partnership provides information to demonstrate otherwise. In at least one case, however, the tax paid may be less. This is where the partnership generates income that would ordinarily be apportioned if earned by nonresidents. In that case, the partnership would apportion the share of the income that flows to indirect partners, even if some of those partners are residents (and would be entitled to a credit for taxes paid to another state, but not to apportioning their income).

During the drafting process, concerns were raised as to whether the partnership-pays election might be used to shift income or avoid state taxes. In particular, the concerns focused on federal partnership adjustments that would be allocated by the electing partnership to “tiered partners.” The model’s provisions to address indirect partners, Section C(3)(b)(iv), discussed above, along with state-specific sourcing rules and equitable apportionment authority, were determined to be sufficient to address these concerns. If a state lacked these other types of authority, however, it might consider adopting such authority for this purpose. This, in turn, might influence the estimate of any revenue impacts.

# Model Uniform Statute for Reporting Adjustments to Federal Taxable Income and Federal Partnership Audit Adjustments

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## SECTION A. Definitions

The following definitions apply for the purposes of [this subdivision of the State Code]:

**(1) “Administrative Adjustment Request”** means an administrative adjustment request filed by a Partnership under IRC section 6227.

**(2) “Audited Partnership”** means a Partnership subject to a Partnership Level Audit resulting in a Federal Adjustment.

**(3) “Corporate Partner”** means a Partner that is subject to tax under [reference to State law].

**(4) “Direct Partner”** means a Partner that holds an interest directly in a Partnership or Pass-Through Entity.

**(5) “Exempt Partner”** means a Partner that is exempt from taxation under [reference to State law] [except on Unrelated Business Taxable Income<sup>1</sup>].

**(6) “Federal Adjustment”** means a change to an item or amount determined under the Internal Revenue Code that is used by a Taxpayer to compute [State tax] owed whether that change results from action by the IRS, including a Partnership Level Audit, or the filing of an amended federal return, federal refund claim, or an Administrative Adjustment Request by the Taxpayer. A Federal Adjustment is positive to the extent that it increases state taxable income as determined under [reference to State laws] and is negative to the extent that it decreases state taxable income as determined under [reference to State laws].

**(7) “Federal Adjustments Report”** includes methods or forms required by [State Tax Agency] for use by a Taxpayer to report Final Federal Adjustments, including an amended [State] tax return, information return, or a uniform multistate report.

**(8) “Federal Partnership Representative”** means the person the Partnership designates for the taxable year as the Partnership’s representative, or the person the IRS has appointed to act as the Federal Partnership Representative, pursuant to IRC section 6223(a).

**(9) “Final Determination Date”** means the following:

(a) Except as provided in Section A(9)(b) and (c), if the Federal Adjustment arises from an IRS audit or other action by the IRS, the Final Determination Date is the first day on which no Federal Adjustments arising from that audit or other action remain to be finally determined, whether by IRS decision with respect to which all rights of appeal have been waived or exhausted, by agreement, or, if appealed or contested, by a final decision with respect to which all rights of appeal have been waived or exhausted. For agreements required to be signed by the IRS and the Taxpayer, the Final Determination Date is the date on which the last party

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<sup>1</sup> Drafting note: This portion of definition should only be used by the [State] if it taxes unrelated business income.



1 signed the agreement.

2 (b) For Federal Adjustments arising from an IRS audit or other action by the IRS, if the  
3 Taxpayer filed as a member of a [combined/consolidated return/report under State law], the  
4 Final Determination Date means the first day on which no related Federal Adjustments arising  
5 from that audit remain to be finally determined, as described in Section A(9)(a), for the entire  
6 group.

7 (c) If the Federal Adjustment results from filing an amended federal return, a federal re-  
8 fund claim, or an Administrative Adjustment Request, or if it is a Federal Adjustment reported  
9 on an amended federal return or other similar report filed pursuant to IRC section 6225 (c),  
10 the Final Determination Date means the day on which the amended return, refund claim, Ad-  
11 ministrative Adjustment Request, or other similar report was filed.

12 **(10) “Final Federal Adjustment”** means a Federal Adjustment after the Final Determination  
13 Date for that Federal Adjustment has passed.

14 **(11) “Indirect Partner”** means a Partner in a Partnership or Pass-Through Entity that itself  
15 holds an interest directly, or through another Indirect Partner, in a Partnership or Pass-Through  
16 Entity.

17 **(12) “IRC”** means the Internal Revenue Code of 1986, as codified at 26 United States Code  
18 (U.S.C.) Section 1, et seq., [insert State’s current practice to incorporate IRC] and applicable regula-  
19 tions as promulgated by the U.S. Department of the Treasury.<sup>2</sup>

20 **(13) “IRS”** means the Internal Revenue Service of the U.S. Department of the Treasury.

21 **(14) “Non-Resident Partner”** means an individual, trust, or estate Partner that is not a Resi-  
22 dent Partner.

23 **(15) “Partner”** means a person that holds an interest directly or indirectly in a Partnership or  
24 other Pass-Through Entity.

25 **(16) “Partnership”** means an entity subject to taxation under Subchapter K of the IRC.

26 **(17) “Partnership Level Audit”** means an examination by the IRS at the partnership level pur-  
27 suant to Subchapter C of Title 26, Subtitle F, Chapter 63 of the IRC, as enacted by the Bipartisan  
28 Budget Act of 2015, Public Law 114-74, which results in Federal Adjustments.

29 **(18) “Pass-Through Entity”** means an entity, other than a Partnership, that is not subject to  
30 tax under [reference to State law imposing tax on C corporations or other taxable entities].

31 **(19) “Reallocation Adjustment”** means a Federal Adjustment resulting from a Partnership  
32 Level Audit or an Administrative Adjustment Request that changes the shares of one or more items

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<sup>2</sup> Drafting note: A State may need to address undefined terms. Suggested language – “To the extent terms used in this [arti-  
cle] are not defined in this Section or elsewhere in [citation to chapter in which this article is contained], it is the intent of the  
Legislature to conform as closely as possible to the terminology used in the amendments to the IRC pertaining to the compre-  
hensive partnership audit regime as contained in the Bipartisan Budget Act of 2015, Public Law 114-74, as amended, and this  
[article] shall be so interpreted.”

of partnership income, gain, loss, expense, or credit allocated to Direct Partners. A positive Reallocation Adjustment means the portion of a Reallocation Adjustment that would increase federal income for one or more Direct Partners, and a negative Reallocation Adjustment means the portion of a Reallocation Adjustment that would decrease federal income for one or more Direct Partners [pursuant to Regulations under IRC section 6225].

**(20) “Resident Partner”** means an individual, trust, or estate Partner that is a resident in [State] under [reference to state laws] for the relevant tax period.

**(21) “Reviewed Year”** means the taxable year of a Partnership that is subject to a Partnership Level Audit from which Federal Adjustments arise.

**(22) “Taxpayer”** means [insert reference to State definition] and, unless the context clearly indicates otherwise, includes a Partnership subject to a Partnership Level Audit or a Partnership that has made an Administrative Adjustment Request, as well as a Tiered Partner of that Partnership.

**(23) “Tiered Partner”** means any Partner that is a Partnership or Pass-Through Entity.

**(24) “Unrelated Business Taxable Income”** has the same meaning as defined in IRC section 512.<sup>3</sup>

## **SECTION B. Reporting Adjustments to Federal Taxable Income – General Rule**

Except in the case of Final Federal Adjustments that are required to be reported by a Partnership and its Partners using the procedures in Section C, and Final Federal Adjustments required to be reported for federal purposes by taking those adjustments into account in the partnership return for the year of adjustment, a Taxpayer shall report and pay any [State] tax due with respect to Final Federal Adjustments arising from an audit or other action by the IRS or reported by the Taxpayer on a timely filed amended federal income tax return, including a return or other similar report filed pursuant to IRC section 6225(c)(2), or federal claim for refund by filing a Federal Adjustments Report with the [State Tax Agency] for the Reviewed Year and, if applicable, paying the additional [State] tax owed by the Taxpayer no later than 180 days after the Final Determination Date.

## **Section C. Reporting Federal Adjustments – Partnership Level Audit and Administrative Adjustment Request**

Except for adjustments required to be reported for federal purposes by taking those adjustments into account in the partnership return for the year of adjustment, and the distributive share of adjustments that have been reported as required under Section B, Partnerships and Partners shall report Final Federal Adjustments arising from a Partnership Level Audit or an Administrative Adjustment Request and make payments as required under this Section C.

### **(1) State Partnership Representative.**

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<sup>3</sup> Drafting note: This term should only be used by the [State] if it taxes unrelated business income.

(a) With respect to an action required or permitted to be taken by a Partnership under this Section C and a proceeding under [reference to provisions for State administrative appeal or judicial review] with respect to that action, the State Partnership Representative for the Reviewed Year shall have the sole authority to act on behalf of the Partnership, and the Partnership's Direct Partners and Indirect Partners shall be bound by those actions.

(b) The State Partnership Representative for the Reviewed Year is the Partnership's Federal Partnership Representative unless the Partnership designates in writing another person as its State Partnership Representative.

(c) The [State Tax Agency] may establish reasonable qualifications for and procedures for designating a person, other than the Federal Partnership Representative, to be the State Partnership Representative.

**(2) Reporting and Payment Requirements for Partnerships Subject to a Final Federal Adjustment and their Direct Partners.** Final Federal Adjustments subject to the requirements of this Section C, except for those subject to a properly made election under Section C(3), shall be reported as follows:

(a) No later than 90 days after the Final Determination Date, the Partnership shall:

(i) File a completed Federal Adjustments Report, including information as required by [State Tax Agency regulation], with [State Tax Agency]; and

(ii) Notify each of its Direct Partners of their distributive share of the Final Federal Adjustments including information as required by the [State Tax Agency regulation]; and

(iii) File an amended composite return for Direct Partners as required under [reference to State law] and/or an amended withholding return for Direct Partners as required under [reference to State law] and pay the additional amount under [reference to State law(s)] that would have been due had the Final Federal Adjustments been reported properly as required.

(b) [Except as provided under State law for minimal tax liabilities]<sup>4</sup>, no later than 180 days after the Final Determination Date, each Direct Partner that is taxed under [reference to State law imposing tax on individuals, trusts, estates, C corporations, etc.] shall:

(i) File a Federal Adjustments Report reporting their distributive share of the adjustments reported to them under Section C(2)(a)(ii) as required under [reference to State laws]; and

(ii) Pay any additional amount of tax due as if Final Federal Adjustments had been properly reported, plus any penalty and interest due under [reference to State law] and less any credit for related amounts paid or withheld and remitted on behalf of the Direct

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<sup>4</sup> DRAFTER'S NOTE: If the state adopts a de minimis rule as further set out in this model, then this section would need to be conditioned on a reference to that rule.

Partner under Section C(2)(a)(iii).

**(3) Election – Partnership Pays.** Subject to the limitations in Section C(3)(c), an Audited Partnership making an election under this Subsection (3) shall:

(a) No later than 90 days after the Final Determination Date, file a completed Federal Adjustments Report, including information as required by the [State Tax Agency rule or instruction], and notify the [State Tax Agency] that it is making the election under this Subsection (3);

(b) No later than 180 days after the Final Determination Date, pay an amount, determined as follows, in lieu of taxes owed by its Direct and Indirect Partners:

(i) Exclude from Final Federal Adjustments the distributive share of these adjustments reported to a Direct Exempt Partner not subject to tax under [reference state law taxing certain income to tax-exempt entities].

(ii) For the total distributive shares of the remaining Final Federal Adjustments reported to Direct Corporate Partners subject to tax under [reference to State law] and to Direct Exempt Partners subject to tax under [reference state law taxing certain income to tax-exempt entities], apportion and allocate such adjustments as provided under [reference to existing multi-state business activity allocation/apportion law or regulation] and multiply the resulting amount by the highest tax rate under [reference to State law(s)];

(iii) For the total distributive shares of the remaining Final Federal Adjustments reported to Non-Resident Direct Partners subject to tax under [reference to State law applying to individuals and /or trusts], determine the amount of such adjustments which is [State]-source income under [reference to existing non-resident partner sourcing law or regulation], and multiply the resulting amount by the highest tax rate under [reference to State law applying to individuals and/or trusts];

(iv) For the total distributive shares of the remaining Final Federal Adjustments reported to Tiered Partners:

(A) Determine the amount of such adjustments which is of a type that it would be subject to sourcing to the [State] under [reference to existing State rules for allocating/apportioning income of non-resident partners]; and then determine the portion of this amount that would be sourced to the state applying [these rules];

(B) Determine the amount of such adjustments which is of a type that it would not be subject to sourcing to the [State] by a Nonresident Partner under [reference to existing State rules for income fully sourced based on a taxpayer's residency];

(C) Determine the portion of the amount determined in Section C(3)(b)(iv)(B) that can be established, under regulation issued by [State Agency], to be properly allocable to Nonresident Indirect Partners or other Partners not subject to tax on the adjustments; or that can be excluded under procedures for Modified Reporting and

Payment Method allowed under Paragraph (5).

(v) Multiply the total of the amounts determined in Section C(3)(b)(iv)(A) and (B) reduced by the amount determined in Section C(3)(b)(iv)(C) by the highest tax rate under [reference to State law applying to individuals and/or trusts];

(vi) For the total distributive shares of the remaining Final Federal Adjustments reported to Resident Direct Partners subject to tax under [reference to State law applying to individuals and /or trusts], multiply that amount by the highest tax rate under [reference to State law applying to individuals and/or trusts];

(vii) Add the amounts determined in Section C(3)(b)(ii), (iii), (v), and (vi), along with penalty and interest as provided in [reference to State law].

(c) Final Federal Adjustments subject to this election exclude:

DRAFTER'S NOTE: THE EXCLUSION IN (i) IS INTENDED TO ADDRESS THE PARTICULAR STATE'S LAW WITH RESPECT TO ADJUSTMENTS THAT WOULD FLOW THROUGH TO CORPORATE PARTNERS AND MIGHT BE TREATED AS PART OF THE UNITARY BUSINESS OF THE CORPORATION.

(i) The distributive share of Final Audit Adjustments that under [reference to State law] must be included in the unitary business income of any Direct or Indirect Corporate Partner, provided that the Audited Partnership can reasonably determine this; and

(ii) Any Final Federal Adjustments resulting from an Administrative Adjustment Request.

(d) {OPTIONAL PROVISIONS}

Option A - An Audited Partnership not otherwise subject to any reporting or payment obligation to [State] that makes an election under this Subsection (3) consents to be subject to [State] laws related to reporting, assessment, payment, and collection of [State] tax calculated under the election.

Option B - An Audited Partnership not otherwise subject to any reporting or payment obligation to [State] may not make an election under this Subsection (3).

**(4) Tiered Partners.** The Direct and Indirect Partners of an Audited Partnership that are Tiered Partners, and all of the Partners of those Tiered Partners that are subject to tax under [reference to State laws imposing tax on individuals, trusts, corporations, etc.] are subject to the reporting and payment requirements of Section C(2) and the Tiered Partners are entitled to make the elections provided in Section C(3) and (5). The Tiered Partners or their Partners shall make required reports and payments no later than 90 days after the time for filing and furnishing statements to Tiered Partners and their Partners as established under IRC section 6226 and the regulations thereunder. The [State Agency] may promulgate regulations to establish procedures and interim time periods for the reports and payments required by Tiered Partners and their Partners

1 and for making the elections under this Section C.

2 **(5) Modified Reporting and Payment Method.** [Drafter's Note: This provision is intended  
3 to allow the state to respond to requests by the partnership for an alternative means of re-  
4 porting that would otherwise satisfy state law requirements for the reporting and payment  
5 of tax and, therefore, the provision allowing the partnership to request a refund to be paid  
6 to the entity should be evaluated by the adopting state in light of whether it would otherwise  
7 conform to state law.] Under procedures adopted by and subject to the approval of the [State  
8 Agency], an Audited Partnership or Tiered Partner may enter into an agreement with the [State  
9 Agency] to utilize an alternative reporting and payment method, including applicable time require-  
10 ments or any other provision of this Section C, if the Audited Partnership or Tiered Partner demon-  
11 strates that the requested method will reasonably provide for the reporting and payment of taxes,  
12 penalties, and interest due under the provisions of this Section C, or if the Audited Partnership or  
13 Tiered Partner can show that their direct partners have agreed to allow a refund of the state tax to  
14 the entity. Application for approval of an alternative reporting and payment method must be made  
15 by the Audited Partnership or Tiered Partner within the time for election as provided in Section  
16 C(3) or (4), as appropriate.

17 **(6) Effect of Election by Audited Partnership or Tiered Partner and Payment of Amount**  
18 **Due.**

19 (a) The election made pursuant to Section C(3) or (5) is irrevocable, unless [State Agency],  
20 in its discretion, determines otherwise.

21 (b) If properly reported and paid by the Audited Partnership or Tiered Partner, the  
22 amount determined in Section C(3)(b), or similarly under an optional election under Section  
23 C(5), will be treated as paid in lieu of taxes owed by its Direct and Indirect Partners, to the  
24 extent applicable, on the same Final Federal Adjustments. The Direct Partners or Indirect Part-  
25 ners may not take any deduction or credit for this amount or claim a refund of the amount in  
26 this State. Nothing in this Subsection(C)(6) shall preclude a Direct Resident Partner from  
27 claiming a credit against taxes paid to this State pursuant to [reference to State law], any  
28 amounts paid by the Audited Partnership or Tiered Partner on the Resident Partner's behalf to  
29 another state or local tax jurisdiction in accordance with the provisions of [State law or regu-  
30 lation allowing credit for taxes paid to another state or locality].

31 **(7) Failure of Audited Partnership or Tiered Partner to Report or Pay.** Nothing in this Sec-  
32 tion C prevents the [State Agency] from assessing Direct Partners or Indirect Partners for taxes they  
33 owe, using the best information available, in the event that a Partnership or Tiered Partner fails to  
34 timely make any report or payment required by this Section C for any reason.

35 **SECTION D. De Minimis Exception**

36 The [State Agency] at its discretion may promulgate regulations to establish a de minimis amount

upon which a taxpayer shall not be required to comply with Sections B and C of this [Chapter].

**SECTION E. Assessments of Additional [State] Tax, Interest, and Penalties Arising from Adjustments to Federal Taxable Income – Statute of Limitations**

The [State Agency] will assess additional tax, interest, and penalties arising from Final Federal Adjustments arising from an audit by the IRS, including a Partnership Level Audit, or reported by the Taxpayer on an amended federal income tax return or as part of an Administrative Adjustment Request by the following dates:

(1) **Timely Reported Federal Adjustments.** If a Taxpayer files with the [State Agency] a Federal Adjustments Report or an amended [State] tax return as required within the period specified in Sections B or C, the [State Agency] may assess any amounts, including in-lieu-of amounts, taxes, interest, and penalties arising from those Federal Adjustments if [State Agency] issues a notice of the assessment to the Taxpayer no later than:

(a) The expiration of the limitations period specified in [citation to State statute setting forth normal limitations period]; or

(b) The expiration of the one (1) year period following the date of filing with the [State Agency] of the Federal Adjustments Report.

(2) **Untimely Reported Federal Adjustments.** If the Taxpayer fails to file the Federal Adjustments Report within the period specified in Sections B or C, as appropriate, or the Federal Adjustments Report filed by the Taxpayer omits Final Federal Adjustments or understates the correct amount of tax owed, the [State Agency] may assess amounts or additional amounts including in-lieu-of amounts, taxes, interest, and penalties arising from the Final Federal Adjustments, if it mails a notice of the assessment to the Taxpayer by a date which is the latest of the following:

(a) The expiration of the limitations period specified in [citation to State statute setting forth normal limitations period]; or

(b) The expiration of the one (1) year period following the date the Federal Adjustments Report was filed with [State Agency]; or

(c) Absent fraud, the expiration of the six (6) year period following the Final Determination Date.

**SECTION F. Estimated [State] Tax Payments During the Course of a Federal Audit**

A Taxpayer may make estimated payments to the [State Agency], following the process prescribed by the [State Agency], of the [State] tax expected to result from a pending IRS audit, prior to the due date of the Federal Adjustments Report, without having to file the report with the [State Agency]. The estimated tax payments shall be credited against any tax liability ultimately found to be due to [State] ("Final [State] Tax Liability") and will limit the accrual of further statutory interest on that amount. If the estimated tax payments exceed the final tax liability and statutory interest ultimately determined to be due, the Taxpayer is entitled to a refund or credit for the excess, provided the

1 Taxpayer files a Federal Adjustments Report or claim for refund or credit of tax pursuant to [citation  
2 to State statute setting forth claim for refund requirements] no later than one year following the  
3 Final Determination Date.

4 **SECTION G. Claims for Refund or Credits of Tax Arising from Final Federal Adjustments Made**  
5 **by the IRS or by Administrative Adjustment Request**

6 Except for Final Federal Adjustments required to be reported for federal purposes by taking those  
7 adjustments into account in the partnership return for the year of adjustment, a Taxpayer may file  
8 a claim for refund or credit of tax arising from Federal Adjustments on or before the later of:

9 (1) The expiration of the last day for filing a claim for refund or credit of [State] tax pursuant  
10 to [citation to State statute setting forth claim for refund requirements], including any extensions;  
11 or

12 (2) One year from the date a Federal Adjustments Report prescribed in Sections B or C, as ap-  
13 plicable, was due to the [State Agency], including any extensions pursuant to Section H.

14 The Federal Adjustments Report shall serve as the means for the Taxpayer, including the Partner-  
15 ship, Tiered Partners, Direct Partners, and Indirect Partners, to report additional tax due, report a  
16 claim for refund or credit of tax, and make other adjustments (including to its net operating losses)  
17 resulting from adjustments to the Taxpayer's federal taxable income. Any refund granted to the en-  
18 tity under Section C is in lieu of state tax that may be owed to the partners.

19 **SECTION H. Scope of Adjustments and Extensions of Time.**

20 (1) Unless otherwise agreed in writing by the Taxpayer and the [State Agency], any adjust-  
21 ments by the [State Agency] or by the Taxpayer made after the expiration of the [State's normal  
22 statute of limitations for assessment and refund] is limited to changes to the Taxpayer's tax liability  
23 arising from Federal Adjustments.

24 (2) The time periods provided for in [this subdivision of the State Code] may be extended:

25 (a) Automatically, upon written notice to [State agency], by 60 days for an Audited Part-  
26 nership or Tiered Partner which has [10,000] or more Direct Partners; or

27 (b) By written agreement between the Taxpayer and the [State Agency] [pursuant to any  
28 regulation issued under this Section].

29 (3) Any extension granted under this Section H for filing the Federal Adjustments Report ex-  
30 tends the last day prescribed by law for assessing any additional tax arising from the adjustments  
31 to federal taxable income and the period for filing a claim for refund or credit of taxes pursuant to  
32 [citation to State statute setting forth claim for refund requirements].

33 **SECTION I. Effective Date**

34 The amendments to this [section/chapter] applies to any adjustments to a Taxpayer's federal taxa-  
35 ble income with a Final Determination Date occurring on and after [date].